Supreme Court of the United States

No. 57

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1961.

No.

ANDREW M. SPHEERIS and ISMENE A. SPHEERIS,
Husband and Wife,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

Petitioner prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Seventh Circuit, entered in the above entitled case on December 13, 1960, Rehearing Denied January 25, 1961.

CITATION TO OPINIONS BELOW

The opinion and findings of fact of the Tax Court of the United States in Docket No. 66548 were filed on November 30, 1959, and the decision was rendered on February 9, 1960, and reported as T.C. Memo 1959-225. On May 5, 1960, pursuant to Section 7482(b) of the Internal Revenue Code, the taxpayers filed a petition for review of the Tax Court decision by the United

States Court of Appeals for the Seventh Circuit, for the reason that the petitioners reside within said Circuit. The opinion of the Court of Appeals for the Seventh Circuit printed as Appendix A hereto, is reported at 284 F. 2d 928.

JURISDICTION

The judgment of the Court of Appeals was entered on December 13, 1960, and Rehearing was denied on January 25, 1961. The jurisdiction of this Court is invoked under 28 U.S.C. Sec. 1254(1).

QUESTION PRESENTED

Are the sums received by the Petitioners in 1953, 1954 and 1955 from the Milwaukee Towne Corporation loans or taxable dividends under Sections 22(a) and 115(a) of the Internal Revenue Code of 1939 and Sections 61(a) 316(a) of the Internal Revenue Code of 1954?

STATUTES INVOLVED

The statutes involved in this appeal are the following: Internal Revenue Code of 1939:

SEC. 115. DISTRIBUTIONS BY CORPORATIONS

(a) Definition of Dividend. — The term "dividend" when used in this chapter (except in section 201 (c)(5), section 204(c)(11), and section 207(a)(2) and (b)(3) (where the reference is to dividends of insurance companies paid by policy holders)) means any distribution made by a corporation to its shareholders, whether in money or in other property, (1) out of its earnings or profits accumulated after February 28, 1913, or (2) out of the earnings or profits of the taxable year (computed as of the close of the taxable year without diminution by reason of any distributions made

during the taxable year) without regard to the amount of the earnings and profits at the time the distribution was made. In the case of a corporation which, under the law applicable to the taxable year in which the distribution is made, is a personal holding company, or which, for the taxable year in respect of which the distribution is made under section 504(c) or section 506, or a corresponding provision of a prior income tax law, is a personal holding company under the law applicable to such taxable year, such term also means any distribution (whether or not a dividend as defined in the preceding sentence) to its shareholders, whether in money or in other property, to the extent of its subchapter A net income, less the sum of the following:

(1) The net operating loss credit provided in section 26(c)(1);

(2) The dividend carry-over provided in section 27(c); and

(3) The deduction for amounts for retirement of indebtedness provided in section 504(b).

Internal Revenue Code of 1954:

SEC. 316. DIVIDEND DEFINED.

(a) General Rule. — For purposes of this subtitle the term "dividend" means any distribution of property made by a corporation to its stockholders—

(1) out of its earnings and profits accumulated after February 28, 1913, or

(2) out of its earnings and profits of the taxable year (computed as of the close of the taxable year without diminution by reason of any distributions made during the taxable year), without regard to the amount of the earnings and profits at the time the distribution was made.

Except as otherwise provided in this subtitle, every distribution is made out of earnings and profits to the extent thereof, and from

the most recently accumulated earnings and profits. To the extent that any distribution is, under any provision of this subchapter, treated as a distribution of property to which section 301 applies, such distribution shall be treated as a distribution of property for the the purposes of this subsection.

STATEMENT OF THE CASE

The material facts are not in dispute. The only dispute between the parties is whether the withdrawals are loans or taxable dividends.

The petitioner is a stockholder and director of the Milwaukee Towne Corp. (formerly the Miller Theater Corporation) and the owner of 117.34 shares of Class A stock, which is less than thirty percent of the total number of shares outstanding of Class A. The Milwaukee Towne Corp.'s outstanding stock in 600 shares, 400 shares of Class A and 200 shares of Class B.

The outstanding stock of the Milwaukee Towne Corp. is as follows (See Exhibit 6-F) (R. 54)

Date Issued	Name	Class	No. of Shares
11/1/46	A. M. Spheeris	A	117 34/100
11/1/46	Mary P. Papas	A	77 22/100
11/1/46	C. J. Papas	A	78 22/100
11/1/46	S. J. Papas	A	78 22/100
11/1/46	John Papas	A	1
11/1/46	B. C. Dolar, Trustee	A	48
11/1/46	United Artists	B	198
11/1/46	Edward Raftery	B	1
11/1/46	Rud. Lohrenz	B	1
9/3/48	Paul Lazarus, Jr.	B	1
9/3/48	Ralph Cramblett	B	1

The petitioner withdrew from the Milwaukee Towne Corp. the following sums:

Year	Amount
1953	$36,500.00
1954	5,000.00
1955	19,500.00

A detailed statement of petitioner's withdrawals as appearing on the books of the Milwaukee Towne Corp. is set forth in Exhibit 12-L. (R. 60)

The respondent has determined that the net withdrawals for 1953, 1954, and 1955 constituted taxable income.

For many years since the organization of the Milwaukee Towne Corp. the petitioner and other stockholders and companies controlled by the stockholders of Milwaukee Towne Corp. loaned money to Milwaukee Towne Corp.; and, similarly, the same parties procured loans from the Milwaukee Towne Corp. The amounts of these loans were recorded on the books of the Milwaukee Towne Corp. and always treated as such. The details of these loans are set forth in the exhibits which are made part of the stipulation, and a summary of these loans is as follows:

LOANS TO COMPANY

From	Balance of Loan Date	Balance of Loan Amount	Date of Repayment	Exhibit
John Papas	8/27/49	$59,842.99	4/30/52	8-H
Andrew M. Spheeris	12/29/48	22,833.33	4/30/52	9-I
United Artists	1/29/49	48,418.37	4/30/52	10-J
Harvard Theatre Corp.	12/5/46	1,000.00	12/26/46	11-K
Woodstock Amusement	12/5/46	7,000.00	12/26/46	11-K
Terminal Restaurant	12/2/46	2,000.00	12/26/46	11-K

LOANS BY THE COMPANY TO STOCKHOLDERS AND OTHERS

To	Period of Loans	Total Loans	Exhibit No.
Andrew M. Spheeris	5/27/53 to 1/31/59	$58,952.73	12-L
S. J. Papas	12/30/53 to 1/31/59	90,500.00	13-M
Frances Papas	8/26/53 to 1/31/59	1,000.00	14-N
Papas Realty	11/14/55 to 1/31/59	34,500.00	15-O
Westgate Outdoor Theatre	9/30/53 to 1/31/59	32,500.00	16-P
Harvard Theatre Corp.	2/24/54 to 1/31/59	4,000.00	17-Q
Keno Family Drive-In Theatre	1/27/54 to 1/31/59	1,750.00	18-R
Woodstock Amusement Corp.	11/25/53 to 1/31/59	7,000.00	19-S

Organization and Litigation Involving the Milwaukee Towne Corp.

The Miller Theatre Corporation, now the Milwaukee Towne Corp., was organized April 11, 1946, and shortly thereafter the management realized that the success of this venture depended on obtaining first-run pictures; United Artists. As a result of these negotiations, two contracts dated June 11, 1946, and an escrow agreement dated September 17, 1946, were entered into, copies of which are attached to Exhibit 25-Y (R. 73) and 26-Z (R. 98). For the purpose of convenience these agreements will be designated:

Agreement No. 1. Stock purchase agreement dated June 11, 1946, attached to Exhibit 25-Y (Exh. A) (R. 73).

Agreement No. 2. Agreement to furnish pictures dated June 11, 1946, attached to Exhibit 26-Z (Exh. II) (R. 98).

Agreement No. 3. Escrow agreement dated September 17, 1946, attached to Exhibit 26-Z (Exh. III) (R. 98).

Agreement No. 1 (Stock Contract) provided that the name of the Miller Theatre Corporation be changed to the Milwaukee Towne Corporation; that the capital stock

be changed to consist of 400 shares of Class A and 200 shares of Class B stock; that the United Artists be permitted to purchase 200 shares of Class B stock; that the 400 shares of Class A stock be purchased by the original stockholders of the Miller Theatre Corporation; and that all of the stockholders would make loans to the Milwaukee Towne Corporation.

Agreement No. 2 (Picture Contract) provided that the United Artists would furnish pictures to the Milwaukee Towne Corporation; and in event of its failure to do so the Milwaukee Towne Corporation could terminate its agreement, and all obligations of the Milwaukee Towne Corporation would be cancelled.

Agreement No. 3 (Escrow Agreement of September 17, 1946), provided that all of the three contracts, namely the stock agreement contract, the agreement to furnish pictures, and the management contract, be deposited with Lazarus Krinsley as escrow agent; and in event a final decree is entered in any Court of competent jurisdiction against the United Artists Corporation declaring the agreements of June 11, 1946, unlawful, then the escrow agent shall tear off the signatures on the agreements, mark the same void, and mail one copy to each party. In event, however, that no such decree was entered within two years after June 11, 1946, then the escrow agent was required to mail one copy of each of said agreements to each of the parties; and said agreements would thereupon become effective as of June 11, 1946.

On September 15, 1948, all of parties to the three agreements, except the United Artists, demanded that the escrow agent tear off the signatures on the agreements and return them to the parties in accordance with the terms of the escrow agreement thereby voiding the agreements. On September 27, 1948, the United Artists

served notice upon the escrow agent directing the escrow agent not to tear off the signatures on the agreements.

On July 14, 1950, the United Artists demanded that the escrow agent deliver to United Artists the agreements; and on the same date C. J. Papas and the other parties to the agreements, except United Artists, demanded that the escrow agent not deliver any of the three agreements to anyone prior to the judicial determination of the rights of the parties under said agreements.

In view of the controversy the escrow agent commenced an action in the United States District Court of Illinois, Case No. 50-C-1024, requesting that the escrow agent be permitted to deliver said three agreements to the Clerk of that Court and abide by the judgment of that Court as to the respective rights of the parties. This case was not decided until 1956 in *Krinsley* v. *United Artists, et al.*, (C.A. 7) 235 F.2d 253, long after the withdrawals.

On June 21, 1954, the Milwaukee Towne Corp. served notice on the United Artists Corporation that the contract to furnish pictures was being terminated. (Copy of notice attached to Exhibit 26-Z)

On September 28, 1954, the petitioner and other stockholders served notice on United Artists demanding that United Artists return the 200 shares of Class B stock. (Copy of notice attached to Exhibit 26-Z) The principal stockholders' contention was that since United Artists did not comply with the picture contract of June 11, 1946, they were not entitled to be stockholders of Milwaukee Towne Corporation.

While this litigation was pending concerning the rights under these three contracts, immediately after the notice of September 28, 1954, the United Artists Corporation on

October 6, 1954, commenced an action against the Milwaukee Towne Corp., its officers and directors in the United States District Court for the Eastern District of Wisconsin, entitled *United Artists Corporation* v. *Milwaukee Towne Corp., et al.*, Case No. 6357 (Exhibit 25-Y). In this action the United Artists Corporation charged that the petitioner and other officers mismanaged the company and that loans and advances had been made to the petitioner and others. In their answer the petitioner and others admitted receiving such loans. This suit was still pending in the United States District Court for the Eastern District of Wisconsin, at the time this case was tried in the Tax Court (but it has since been settled).

It was under these conditions, climate and relationship between Milwaukee Towne Corp., its officers and directors and the United Artists Corporation, a belligerent minority stockholder, that these withdrawals were made, which the respondent chooses to designate as dividends.

REASONS FOR GRANTING WRIT

I. The decision below fails to consider and apply the correct standard adopted by the Supreme Court for determining individual income taxable under the pertinent statutes. Based upon the established facts of record, the application of the "claim of right" rule requires a decision favorable to the petitioner.

Whether or not funds obtained by the stockholder from the corporation is to be classified as income for purposes of taxation is ultimately to be determined by the intent of the parties at the time of the transfer. Although there is no single standard for absolute determination of this intent, the Supreme Court has for a number of years applied the accepted standard as stated

by Justice Brandeis in *North American Oil Consolidated* v. *Burnet*, 286 U.S. 417, 424, 52 S. Ct. 613, 76 L. Ed. 1197 (1932):

> "If a taxpayer receives earnings under *a claim of right* and without restriction as to its disposition, he has received income which he is required to return . . ." (Italics ours.)

In the case at bar it was clear that the taxpayer did not receive these withdrawals under any claim of right, nor did he claim that he had a right to these withdrawals as dividends. In fact he admitted, long before the Government raised any questions as to whether these withdrawals were dividends (Def. Notice issued 1/8/57) that he had no right to these withdrawals as dividends but that they were loans. In his answer in *United Artists Corporation* v. *Milwaukee Towne Corp., et al.*, Case No. 6357, United States District Court for the Eastern District of Wisconsin (Exhibit 26-Z), which he filed on October 7, 1954 (R. 98-117), taxpayer admitted that any withdrawals he made from the Milwaukee Towne Corporation were loans and not dividends.

This standard, sometimes called the "claim of right" rule has been consistently applied by the Supreme Court and followed in the decisions of the lower courts. In determining what is taxable income, in the case of *Commissioner of Internal Revenue* v. *Wilcox*, 327 U.S. 404, 66 S. Ct. 546, 548, 549, 90 L.Ed. 752 (1946), the Court decided that there must be two elements, namely, (1) the presence of a claim of right to the alleged gain, and (2) the absence of a definite, unconditional obligation to repay or return that which would otherwise constitute a gain. The Supreme Court commented in the *Wilcox* case as follows:

"Not every benefit received by a taxpayer from his labor or investment necessarily renders him taxable. Nor is mere dominion over the money or property decisive in all cases. . . For present purposes, however, it is enough to note that a taxable gain is conditioned upon (1) the presence of a claim of right to the alleged gain and (2) the absence of a definite, unconditional obligation to repay or return that which would otherwise constitute a gain. Without some bona fide legal or equitable claim, even though it be contingent or contested in nature, the taxpayer cannot be said to have received any gain or profit within the reach of Section 22(a). See *North American Oil* v. *Burnet*, 286 U.S. 417, 424, 52 S. Ct. 613, 615, 76 L.Ed. 1197. Nor can taxable income accrue from the mere receipt of property or money which one is obligated to return or repay to the rightful owner, as in the case of a loan or credit." (Emphasis supplied.)

This standard for determining taxable gain requires proof not only of (1) the presence of a claim of right by the taxpayer to the alleged gain, but also, (2) the absence of a definite, unconditional obligation to repay or return the fund.

In the case at bar there was no "claim of right" as to the alleged dividends and a definite obligation to repay was evidenced by the admission of the taxpayer in the answer in *United Artists Corporation* v. *Milwaukee Towne Corp., supra*, the taxpayer's testimony before the Tax Court, and the books of the account of the Milwaukee Towne Corporation showing that these withdrawals were recorded on the books of the corporation as loans receivable from the petitioner.

The Supreme Court in *Healy* v. *Commissioner of Internal Revenue*, 345 U.S. 278, 73 S.Ct. 671, 674, 97 L.Ed. 1007 (1953), recognized the application of the standard and commented upon the phrase "claim of right":

> "The phrase 'claim of right' is a term known of old to lawyers. Its typical use has been in real property law in dealing with title by adverse possession, where the rule has been that title can be acquired by adverse possession only if the occupant claims that he has a right to be in possession as owner. The use of the term in the field of income taxation is analogous. There is a claim of right when funds are received and treated by a taxpayer as belonging to him."

This quotation from the *Healy* decision points out that "there is a claim of right when funds are received and treated by a taxpayer as belonging to him." When the Court referred to funds received and treated by taxpayer as belonging to him, the Court did not necessarily mean how or for what purpose the taxpayer used these funds. In referring to the funds as being treated as belonging to him, the Court meant that he could use these funds as his sole property and without being required to repay same. While a borrower may treat funds as though they belonged to him for the purpose of disbursements, unless there is a specific provision with reference to the purpose of the disbursement, nevertheless such funds are not free from the repayment obligation as required by the "claim of right" rule.

In the present case the petitioner and the corporation both understood that the withdrawn funds constituted a loan. The petitioner never claimed that he held the funds free of the indebtedness. The evidence in the record all indicates that petitioner always recognized an obligation to make repayment of the loan to the corporation.

In *North American Oil Consolidated* v. *Burnet*, 286 U.S. 417, 424, 52 S. Ct. 613, 76 L. Ed. 1197 (1932), the Supreme Court stated: "if a taxpayer receives earnings under a claim of right and without restriction as to its disposition

he has received income which he is required to return." Although petitioner was free to use the funds withdrawn as he pleased he did not hold them "without restriction" with respect to repayment, as the funds were always subject to being repaid.

The court below erred in failing to apply the "claim of right" rule, as expressed by the Supreme Court. Petitioner pointed out in its appellate brief to the court below that the Tax Court was in error in basing its decision upon standards contrary to the decided cases.

> "The Tax Court decision is erroneous because its findings of fact are contrary to and not sustained by the evidence and its conclusion of law is contrary to the decided cases." (Petitioner's Court of Appeals brief page 44).

Neither the Tax Court opinion or the decision of the Court of Appeals applied the "claim of right" rule. They are in error in their failure to do so.

II. The failure of the decision below to consider and apply the "claim of right" standard, conflicts with decisions within closely related areas from the same circuit and from a number of the other courts of appeals.

The "claim of right" rule has been applied as a standard for determining taxable individual income in a number of Court of Appeals including the Court of Appeals for the Seventh Circuit. In *Bates Motor Transport Lines v. Commissioner of Internal Revenue*, 200 F. 2d 20, 23, 24 (7th Cir. 1952), the court stated:

> "In considering the contention on behalf of taxpayer Bates, we must keep in mind the principle announced by the Supreme Court in North American Oil Consolidated v. Burnet, 286 U.S. 417, wherein it was said on page 424, 52 S. Ct. 613, on page 615, 76 L. Ed. 1197:

"If a taxpayer receives earnings under a claim of right and without restriction as to its disposition, he has received income which he is required to return, even though it may still be claimed that he may still be adjudged liable to restore its equivalent.'"

"That principle was confirmed and followed in United States v. Lewis, 340 U.S. 590, 71 S. Ct. 522, 95 L. Ed. 560."

In applying this test to the facts under consideration the Court stated in the *Bates* case, *supra,* at page 24:

"In both the case now under consideration and the Rock Island case, there was a fixed and definite legal obligation to refund. In the Rock Island case the obligation to refund and the amount of refund was definite and fixed, the only uncertainty was in respect to the person to whom such refund was to be made. The obligation to refund in that case was imposed by law; it was quasi contractual in its nature.

"In the case at bar the obligation to repay and the person to whom the refund is to be made are definite and fixed, the only uncertainty arises from the amount of refund which was to be ascertained by the General Accounting Office on audit. The obligation to refund was contractual, it arose from the 'Standard Motor Freight land grant equilization agreement' signed by the taxpayer."

Since the Seventh Circuit in *Bates Motor Transport Lines* v. *Commissioner of Internal Revenue, supra,* held that where there is an obligation to repay the amount repayable cannot be considered taxable income, then why does not this doctrine of law apply to the instant case?

Examples of the application of the "claim of right" rule in related fact situations within decisions from the Court of Appeals of other Circuits include: *Hedrick* v.

Commissioner of Internal Revenue, 154 F. 2d 90, 91 (2nd Cir. 1946).

> "His clear right and unhampered opportunity to do as he would with what was due him fixed the tax consequences. As was said in Corliss v. Bowers, 281 U.S. 376, 50 S. Ct. 336, 337, 74 L. Ed. 916, 'The income which is subject to a man's unfettered command and that he is free to enjoy at his own option may be taxed to him as his income, whether he sees fit to enjoy it or not.'"

In the case at bar Spheeris was not free to enjoy the withdrawals as his own—he was required to repay these withdrawals.

Fleischer v. *Commissioner of Internal Revenue*, 158 F. 2d 42, 44 (8th Cir. 1946):

> "What they received in that year as salaries from the corporation they received without restriction and under a claim of right. They accepted these salaries as income and reported them as such."

See also, *Drybrough* v. *Commissioner of Internal Revenue*, 238 F. 2d 735 (6th Cir. 1956); *Beacon Publishing Co.* v. *Commissioner of Internal Revenue*, 218 F. 2d 697 (10th Cir. 1955).

The present decision, *Spheeris* v. *Commissioner of Internal Revenue*, 284 F. 2d 928, (7th Cir. 1960), states at p. 931:

> "In cases involving payments to stockholders, subsequent to advances to their corporation, where it is disputed whether such advances were loans or capital contributions, we have held that the subjective intention of the parties is a major factor in determining the legal relationship for tax purposes. Jennings v. United States, 7 Cir. 1959, 272 F. 2d 842. Ortmayer v. C.I.T. supra. Such intention may be ascertained

> from the testimony of witnesses and from objective manifestations of intent. No single indicium or criterion is conclusive. Arlington Park Jockey Club v. Sanuber, 7 Cir. 1959, 262 F. 2d 902. Similarly here, the legal relationship between the closely-held corporation and its stockholders as to these particular payments must be established by a consideration of all revelant factors including the true intent of the parties."

The three cases cited by the Court of Appeals, *Arlington Park Jockey Club* v. *Sauber*, 262 F. 2d 902 (7th Cir. 1959); *Ortmayer* v. *C.I.T.*, 265 F. 2d 848 (7th Cir. 1959); *Jennings* v. *United States*, 272 F. 2d 842 (7th Cir. 1959), all involved a different issue, namely, whether the funds were loans to the corporation or capital investment by the taxpayer. Although the broad statements contained therein and relied upon in the present decision are of general application, they do not apply here since the "claim of right" was not involved with respect to the funds in those cases—consequently, there is no justification for failure to apply the well established "claim of right" rule as promulgated by the Supreme Court. It is submitted that the standard applied by the Circuit Court of Appeals for the Sixth Circuit in *Lashells' Estate* v. *Commissioner of Internal Revenue*, 208 F. 2d 430, 435 (6th Cir. 1953), should have governed and is applicable in the present case:

> "It is well established that the mere receipt and possession of money does not by itself constitute taxable income. Familiar examples are borrowed money, rent collected by a rental agent, payment of a loss under an insurance policy, and a money judgment collected by an attorney for a claimant. Using the concept of taxable income, the Supreme Court adopted the 'claim of right' rule for the purpose of

> determining whether the receipt and possession of money constituted income. . . . The absence of an enforceable obligation to pay the money to someone else is only one of the two conditions necessary to constitute income. There must also exist a 'claim of right' on the part of the taxpayer. The performance of the agreement, whether legally enforceable or not, negatives the 'claim of right.'"

In the case at bar all the uncontradicted evidence is to the effect that these withdrawals were loans and the petitioner was legally obligated to repay these.

The failure of the Court to apply the proper standard, namely, the "claim of right" test, produced an incorrect conclusion of ultimate fact. This same error was also involved in the Tax Court opinion. It was never considered by the Court, much less established, that the petitioner ever indicated either expressly or by implication that he was withdrawing the funds under a personal claim of legal right to them as against the interest of the corporation. In addition, in order to establish that the funds withdrawn by the petitioner were properly to be classified as a taxable gain, it must be established that there was no obligation to repay or return the funds. This was not established here.

The uncontested evidence indicates that the withdrawals were obtained by the petitioner under a consentual agreement including an obligation to repay the funds to the corporation. The funds were not taken under a "claim of right" to absolute ownership as against the corporation.

The Tax Court has heretofore held that the withdrawals which are required to be repaid are not income and, therefore, such withdrawals under the decided cases are not taxable income. This is especially true when the

taxpayer's claim of debt is buttressed by evidence, as here, that the withdrawals were charged to petitioner as accounts receivable on the corporate books.

In *Fred T. Wood,* 27 B.T.A. 162 (1932), the Board of Tax Appeal stated at page 166:

> "Therefore, if the corporation had become insolvent, creditors might have required petitioner to pay into the corporation the amount shown as owing to it on his account; or, if by reason of a new venture or an expansion of business, the corporation needed additional funds, which were furnished by petitioner and credited on his account it would not have constituted a contribution to capital but a payment of his indebtedness to the corporation. Harry E. Wiese, 35 B.T.A. 701, 705 (1937) affd. Wiese v. Commissioner of Internal Revenue, 93 F. 2d 921 (8th Cir. 1938) cert. denied, 304 U.S. 562, 58 S. Ct. 944, 82 L. Ed. 1529, rehearing denied, 304 U.S. 589, 58 S. Ct. 1045, 82 L. Ed. 1549.
>
> "The only purpose of maintaining the existence of the subsidiary was to undertake future Canadian contracts. The petitioner did not know when such a contract might be procurred and it might become necessary to restore the fund withdrawn, or some part thereof, to finance the contract. . . . As pointed out in Commissioner v. Cohen, 77 F. 2d 184, if no dividends had been declared and the subsidiary had become insolvent, the payments would have been recoverable by its creditors. Wilputte Coke Oven Corporation, 10 T.C. 435, 443 (1948).
>
> "This record discloses no reason why the amounts charged to petitioner should not be regarded as accounts receivable from him as reflected by the books, notwithstanding the fact that the conduct of the corporate business was exceedingly informal. The company might have undertaken a new venture —its powers were sufficiently broad—and called upon petitioner for payment; former stockholders might

have demanded pro rata payment of the funds retained by petitioner; creditors of the corporation might have required repayment—such occurrences were possible during the course of the company's operation." See also, Carl L. White, 17 T.C. 1562, at 1568 (1952).

The failure of the court below to give consideration to the fact that the petitioner was obligated to repay the funds withdrawn clearly establishes that both the Tax Court and the Court of Appeals failed to take into account the "claim of right" rule. It indicates a failure to follow the standards for determining taxable individual income as determined by the Supreme Court in *North American Oil Consolidated* v. *Burnet, supra; Commissioner of Internal Revenue* v. *Wilcox, supra; Healy* v. *Commissioner of Internal Revenue, supra.*

In *Commissioner of Internal Revenue* v. *Wilcox,* 327 U.S. 404, 408-409, 66 S. Ct. 546, 90 L. Ed. 752 (1946), the taxpayer-employee embezzled funds from his employer. In holding that these funds did not constitute taxable income to the employee under section 22(a) of the Internal Revenue Code, the Supreme Court stated:

> "It is obvious that the taxpayer in this instance, in embezzling the $12,748.60, received the money without any semblance of a bona fide claim of right. And he was at all times under an unqualified duty and obligation to repay the money to his employer. . . . The employer, moreover, at all times held the taxpayer liable to return the full amount. The debtor-creditor relationship was definite and unconditional."

There is a similar definite and unconditional debtor-creditor relationship between petitioner and the corporation in the present case. The embezzler in the *Wilcox* case did not take the funds under any claim of right.

Neither did the present petitioner here withdraw corporate funds under a claim of right without legal obligation to repay the loan. The Supreme Court, in the above quotation, points out that the embezzler is under an unqualified duty and obligation to repay the money to his employer. Petitioner, in the present case, has always admitted that there is an unqualified obligation on his part to repay the loans to the corporation. On page 54 of petitioner's appellate brief to the court below it was pointed out that:

> "We admit that if the petitioner could decide whether he would or would not repay these withdrawals, then there would be justification for holding that these were dividends rather than loans. However, the Tax Court recognizes that repayment was not within the control of the petitioner when he stated 'unless he choose or was forced to do so.' This clearly establishes that these withdrawals legally were loans and not dividends. Further evidence of this is that petitioner admitted that these were loans, in the action commenced by the United Artists in 1954. United Artists Corporation v. Milwaukee Towne Corporation, Case No. 6357, Eastern District of Wisconsin. This was an admission against interest and clearly established a legal obligation to repay."

In the *Wilcox* case the Supreme Court pointed out that the employer at all times held the taxpayer liable to return the full amount of the fund taken. Similarly, in the present case, the corporation has never released the petitioner from his admitted obligation of repayment of the withdrawn funds. In the *Wilcox* case the court applied the "claim of right" rule and determined that the funds obtained by the taxpayer were not taxable to him as income. The Court below in the present case should have applied the same test with the same result.

The Court of Appeals in this case was in error in failing to apply the standards set forth by the Supreme Court in *North American Oil Consolidated* v. *Burnet*, or the *Wilcox* or *Healy* decisions. Under the standards and rule of law as established by these decisions, the withdrawals in question are not taxable income under Section 115(a) IRC 1939, and Section 316(a) IRC 1954.

III. The decision below is based upon a series of negative implications rather than positive proof. Each of these negative implications have been held by courts in related fact situations not to justify the conclusion that the fund in question constitutes individual income for tax purposes.

In the present opinion the Court of Appeals states, *Spheeris* v. *C.I.R.*, 284 F. 2d 928, 931 (1960):

> "After examination of the relevant facts, we agree with the Tax Court that the legal effect of the payments in question was to provide dividends to Spheeris. Numerous objective facts support this conclusion: None of the withdrawals was evidenced by promissory notes or secured by collateral; no interest was charged or paid; no dates for repayment were set and the single repayment came after the instant proceeding was initiated; no dividends were declared, but withdrawals were taken from the closely-controlled corporation as Spheeris and his family needed funds; and finally, prior loans made to Towne were evidenced by promissory notes and repaid with interest."

The Court designated objective facts in support of its conclusion, namely:

1. None of the withdrawals were evidenced by promissory notes.
2. No interest was charged or paid.

3. No dates for repayment were set.

4. No dividends were declared.

It is submitted that each of these contentions constitute merely negative implications.

(1) None of the withdrawals were evidenced by promissory notes or secured by collateral.

An obligation does not have to be evidenced by a note, and there is certainly no requirement that collateral must be given before a debt is created. As stated by the Tax Court in *A. J. Dalton*, T. C. Memo 1957-020:

> "There is nothing unusual about a corporation's loaning money to its stockholders without security, notes or interest."

In *Leonard J. Erickson*, T. C. Memo 1956-256, the Tax Court commented:

> "We are not impressed by respondent's reliance upon the absence of written evidence of indebtedness or of security at the outset. The lenders expected at least the major portion of the advances to remain outstanding only for a short period and together they controlled the corporation directly, or indirectly through their families. The foregoing facts rob the initial absence of notes and the informality of the transaction of much of the significance which respondent purports to see therein."

(2) No interest was charged or paid.

Again we have merely a negative inference. It is not necessary that an indebtedness involve the payment of interest, any more than that it be secured by collateral. Evidence that interest was not paid on the amount withdrawn does not tend to establish that the parties intended the funds to be free of repayment obligation. On several

occasions the Tax Court has pointed out that the failure to pay interest is not determinative. In *Victor Shaken*, 21 T.C. 785, 793, (1954) the court stated:

> "The failure to charge interest is not determinative here. See Irving T. Bush, 45 B.T.A. 609, 623, remanded without consideration of this point (C.A. 2), 133 F. 2d 1005. Petitioner's execution of a note in 1949 for the net balance due and the carrying of the amounts on the books of the corporation as loan receivables cannot be ignored. See Moses W. Faitoute, 38 B.T.A. 32, 35."

The fact that no note was issued is no proof that there was no intention to repay or no requirement of repayment. *Appeal of Kate C. Ryan, Executrix*, 2 B.T.A. 1130, *F. A. Wilson*, 46,177 T.C. Memo (July 1946); and *Harry E. Wiese* v. *Commissioner*, 35 B.T.A. 701, Affd. 93 F.2d 921.

(3) No dates for repayment were set and the single repayment came after the instant proceedings were initiated.

The fact that the transactions between the corporation and petitioner were informal in nature and did not include a specified date for repayment does not establish the nature of the transaction.

> *Al Goodman, Inc.*, 23 T.C. 288 (1945): "On the state of the record we deem it of no significance that the withdrawals were not formally authorized by the directors or that no interest was charged thereon. Irving T. Bush, supra." See also, Leonard J. Erickson, supra.

All of the positive facts, *i.e.*, the account entries in Towne's books, the relationship of withdrawals to proprietary interest, the 1954 mismanagement suit, and the

testimony of all interested parties, serve to establish that the funds were not withdrawn with the intent that they should constitute income to petitioner in the form of corporate dividends. In contrast, each of the factors relied upon by the court below creates, at best, merely a negative inference. Petitioner clearly established a mutual intent to withdraw the funds as loans. The court below is in error in failing to give recognition to this fact.

(4) No dividends were declared.

The fact that the stockholder has sufficient control that he may withdraw funds from the corporation without the formality of executing a note and paying interest does not establish that the parties did not intend the withdrawals as a loan, especially in light of the testimony of the parties, the accounting entries on Towne's books, and the fact that the withdrawals were not in proportion to the stockholder's proprietary interest. The Tax Court in *Al Goodman, Inc.*, 23 T.C. 288, 300, (1954), in holding that money withdrawn by controlling stockholders was not necessarily dividends, stated:

> "Al and Ethel were in effect the sole stockholders of the corporation and Al was in complete control of its operation. That this fact is not controlling, as well as the correct test to be applied in determining the instant question, was set forth by us in Carl L. White, 17 T.C. 1562, 1568: 'The important fact is not petitioner's measure of control over the company but whether the withdrawals were in fact loans at the time they were paid out. Wiese v. Commissioner, (C.A. 8, 1938, 93 F. 2d 921, 923, certiorari denied, 304 U.S. 562, rehearing denied 304 U.S. 589 (1938).) The character of the withdrawals depends upon the petitioner's intent and whether he took the company's money for permanent use in lieu of dividends or whether he was then only borrowing it."

In *Wiese* v. *Commissioner of Internal Revenue*, 93 F. 2d 921, (8th Cir. 1938), certiorari denied 304 U.S. 562, 58 S. Ct. 944, 82 L. Ed. 1529, rehearing denied 304 U.S. 589, 58 S. Ct. 1045, 82 L. Ed. 1549, (1938), the petitioner owned all of the corporate stock, no minute books were ever kept by the corporation, except for the first meeting, and no dividends were ever declared by the corporate board of directors. The corporate books carried an account in petitioner's name to which were debited all withdrawals made by the petitioner except salary payments. No notes were signed for the funds withdrawn and charged to the account, and no interest was paid on the funds withdrawn. In affirming the Tax Conrt finding that during the periods of withdrawal these funds constituted loans to the petitioner, the Court of Appeals stated, 93 F. 2d 921, 923 (8th Cir. 1938):

> "During that period he did not report the withdrawals as income, but they were carried on the books of his corporation as accounts receivable. The finding of the board is therefore supported by substantial evidence . . . The significant fact in the present case was the intent of the petitioner when he took the money, whether he was then only borrowing. The intent must be inferred from the conduct of the petitioner, since there is no other evidence of it . . . We can find in the stipulation no facts from which we can say that the Board of Tax Appeals should, as a matter of law, have inferred that the petitioner intended his withdrawals to be permanent at the time he had made them."

In *Cohen* v. *Commissioner of Internal Revenue*, 77 F. 2d 184 (6th Cir. 1935), the petitioners as stockholders of the corporation had an account with the corporation to which was charged as a debit all cash withdrawals. The Court of Appeals, in holding that these withdrawals were loans at the time of their withdrawal stated:

"There was no agreement between the stockholders and no corporate action declaring the character of these withdrawals. However, there was no evidence of any distribution by the corporation prior to the adoption of the resolution of 1928. Moreover, there is evidence that when the sums withdrawn were in excess of the credits, a debt was created. This inference arises from the very nature of a drawing account. Also, it is significant that the withdrawals were not in proportion to the stock ownership." (Emphasis added.)

In *Sala* v. *Commissioner of Internal Revenue*, 146 F.2d 228, 229 (2nd Cir. 1944), Laura Sala, the stockholder in two corporations, borrowed from the corporations between 1927 and 1932 approximately two million dollars. The corporation in 1935 wrote off these debts as uncollectable. Both the Commissioner and the Tax Court held that these withdrawals were taxable dividends. The Circuit Court reversed. The Court held that such withdrawals from the corporation by the sole stockholder did not constitute taxable income to her in the year in which corporation action was taken to write off such debts so far as uncollectable but not purporting to release the indebtedness. The court commented upon the effect of such corporate resolution, at page 229:

"Except in that case (where the debt is in the form of a note which the corporation delivers to the maker for cancellation) we cannot believe that if, for example, the corporation later went bankrupt, the creditors would be barred from collecting the debt from the shareholder. Nor can the doctrine rest upon Higgins v. Smith, 308 U.S. 473, 60 S. Ct. 355, 84 L. Ed. 406, which held that when a sole shareholder deals with his corporation, the Treasury may at its pleasure disregard the form, or insist upon it. Cer-

tainly it has never been held that, when it does insist, the transaction will have other legal consequences than the law would attach to it, if it had been between the taxpayer and a stranger."

These observations are pertinent to the present case. If the form of the transaction, and the legal consequences that would have attached if the transaction had involved the taxpayer and a stranger, can not be disregarded by the government under the facts of the *Sala* decision, then certainly should not have been disregarded in the present case. In the *Sala* case, as contrasted with the present one, the petitioner was the sole stockholder in the corporation. In the *Sala* case there was a corporate resolution writing off Sala's obligation so far as it was felt to be uncollectable. In the present case no comparable resolution has ever been passed by the corporation, and petitioner at all times recognizes his indebtedness to the corporation.

The issue in the present case is one of serious importance. Its impact extends beyond the individual petitioner within the present litigation. Where, as here, both the corporation and Spheeris have always contended that these withdrawals constitute a loan, when the corporate books so indicate, where the petitioner on October 7, 1954, admitted in a verified answer that these were loans, which was long before the additional tax was imposed (Def. Notice issued 1/8/57—R. 6-11), and all other affirmative testimony supports the contention that these were loans, for the government to maintain that this was taxable income, such position is contrary to the intent of the income tax law since Congress intended to tax only income and not loans.

IV. The Tax Court findings are conclusions of law and are reviewable by the Appellate Court below. The Appellate Court is in error in its position that they are not called upon to determine whether the facts find sufficient support with the record.

The opinion of the appellate court below includes the following comment:

> "In reviewing the Tax Court's determining that the payments in question were taxable dividends, the problem before us involves 'mixed questions of law and fact.' We may review the legal effect of the facts found by the trier of fact. Ortmayer v. C.I.R., 7 Cir., 1959, 265 F. 2d 848, 854. The primary facts here were not in dispute, *and we are not called upon to determine whether they find sufficient support in the record or are clearly erroneous* as was the situation in Zeddies v. C.I.R., 7 Cir., 1959, 264 F. 2d 120, 126." (Emphasis supplied.)

Ultimate facts have been held to be conclusions of law. The Tax Court holding as an ultimate fact that the withdrawals were dividends resulted in a conclusion of law. The appellate court below is, therefore, in error in stating that it is not called upon to determine whether the primary facts find sufficient suport within the record. The basis of a conclusion of law is subject to such review. If such review had been made, it would clearly disclose and compel the conclusion that the Tax Court's. finding that the withdrawals were dividends, rather than loans, was not supported by the evidence in the record. All of the affirmative evidence in this record indicates clearly that the withdrawals were intended as loans. The position adopted by the Court of Appeals that it was not required to review the ultimate facts is contrary to the decisions.

CONCLUSION

The decision of the Court of Appeals is in error in that it failed to apply the "claim of right" rule for determining whether the withdrawals in question were dividends or a loan. This rule has been recognized and applied by the Supreme Court in closely related areas in a number of recent decisions. *Commissioner of Internal Revenue* v. *Wilcox*, 327 U.S. 404 (1946); *Healy* v. *Commissioner of Internal Revenue*, 345 U.S. 278, rehearing denied 345 U.S. 961 (1953). It has been followed in decisions from most of the Circuit Court of Appeals, including the Seventh Circuit. *Bates Motor Transport Lines* v. *Commissioner of Internal Revenue*, 200 F. 2d 20, 23, 24 (7th Cir. 1952).

It is submitted that if the "claim of right" rule had been correctly applied in the present case the Court would have been compelled to conclude that the withdrawals did not constitute a taxable dividend, as the evidence establishes that the funds in question were not withdrawn under a claim of right of absolute ownership, nor with intent that petitioner could exercise control and retain the benefit as owner free of legal obligation to repay the funds to the corporation.

In contrast to the application of the above stated legal rule for determination of intent of the parties, the Court of Appeals, in reaching its conclusion that the opinion of the Tax Court should be affirmed, refers to a series of factors, which it classified as operative facts, but which are actually only negative inferences. Although the petitioner has the burden of proof of showing the invalidity of the Tax Court opinion, it is submitted that the rule of

law established under the claim of right, which has been applied in similar cases by the Court of Appeals for the Seventh Circuit and other Courts of Appeal and repeatedly adopted by the Supreme Court, is sufficient to establish that the decision of both the Tax Court and the Court of Appeals was contrary to law.

For these reasons, the petition for writ of certiorari to the United States Court of Appeals for the Seventh Circuit should be granted.

Dated, this 14th day of April, 1961.

Respectfully submitted,

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APPENDIX A.

Opinion.

IN THE
UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

SEPTEMBER TERM AND SESSION, 1960.

No. 13093
ANDREW M. SPHEERIS and
ISMENE A. SPHEERIS,
Petitioners,
v.
COMMISSIONER OF INTERNAL REVENUE,
Respondent.

On Petition for Review of the Decision of the Tax Court of the United States.

December 13, 1960.

Before HASTINGS, *Chief Judge*, SCHNACKENBERG and CASTLE, *Circuit Judges*.

HASTINGS, *Chief Judge*. This petition to review a decision of the Tax Court of the United States raises one central issue—the legal characterization for income tax purposes of certain payments made by Milwaukee Towne Corporation (Towne) to taxpayer Andrew M. Spheeris. Spheeris and his wife Ismene, joint taxpayers and petitioners, here contend that such payments were loans by the corporation to them and as such were not reportable income. The Commissioner argues that the payments were dividends and therefore constituted taxable income. The Tax Court held that the payments in question were divi-

dends within the relevant statutes[1] and assessed deficiencies in petitioners' income tax for the calendar years 1953, 1954 and 1955 in the respective amounts of $18,908.66, $5,592.76, and $8,486.00.

The pertinent factual background of this case, as revealed in unchallenged findings of the Tax Court, may be summarized as follows.

In 1946, the Miller Theater Corporation was organized in Wisconsin by Andrew Spheeris and two brothers-in-law, C. J. Papas and S. J. Papas. The three divided the capital stock equally. Shortly thereafter, pursuant to an agreement with United Artists Corporation, the Miller Theater Corporation was reorganized to form the Milwaukee Towne Corporation. United Artists agreed to furnish Towne with motion pictures; in turn, it was permitted to purchase 200 shares of Towne's Class B stock. It further agreed to make loans to Towne. The 400 shares of Class A stock in Towne were to be purchased by the former owners of the Miller Theater Company.

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[1]Internal Revenue Code of 1939, Sec. 115. Distributions by Corporations.

"(a) Definition of Dividend.—The term 'dividend' when used in this chapter * * * means any distribution made by a corporation to its shareholders, whether in money or in other property, (1) out of its earnings or profits accumulated after February 28, 1913, or (2) out of the earnings or profits of the taxable year (computed as of the close of the taxable year without diminution by reason of any distribution made during the taxable year), without regard to the amount of the earnings and profits at the time the distribution was made." 26 U.S.C.A. § 115 (1952 ed.)

Internal Revenue Code of 1954, Sec. 316. Dividend Defined.

"(a) General Rule.—For purposes of this subtitle, the term 'dividend' means any distribution of property made by a corporation to its shareholders—

(1) out of its earnings and profits accumulated after February 28, 1913, or

(2) out of its earnings and profits of the taxable year (computed as of the close of the taxable year without diminution by reason of any distribution made during the taxable year), without regard to the amount of the earnings and profits at the time the distribution was made.

Except as otherwise provided in this subtitle, every distribution is made out of earnings and profits to the extent thereof, and from the most recently accumulated earnings and profits. To the extent that any distribution is, under any provision of this subchapter, treated as a distribution of property to which section 301 applies, such distribution shall be treated as a distribution of property for purposes of this subsection." 26 U.S.C.A. § 316 (1958 ed.)

The authorized capital stock of Towne has been held since November, 1946 as follows:

Name	Class	No. of Shares
A. M. Spheeris	A	117 34/100
Mary J. Papas	A	77 22/100
C. J. Papas	A	78 22/100
S. J. Papas	A	78 22/100
John Papas	A	1
B. C. Dolar, Trustee	A	48
United Artists	B	198
Edward Raftery	B	1
Rud. Lohrenz	B	1
Paul Lazarus, Jr.	B	1
Ralph Cramblett	B	1

Since 1946, the ownership of all 400 shares of Class A stock, except for 48 shares held in trust for United Artists, has been in the hands of Spheeris and his family who have operated Towne as a close family unit.

During the years 1946-1949, Towne received substantial loans from various sources, including Spheeris, his father-in-law John Papas, United Artists, and other corporations. All these loans, which were repaid by Towne by mid-1952, were evidenced by promissory notes and bore interest of four per cent.

Beginning in 1953, Spheeris and other stockholder-members of his family withdrew funds from Towne for their personal use. No withdrawals were made on behalf of United Artists. Corporations which Spheeris and members of his family controlled also received funds from Towne during this period. It is indicated that such withdrawals were *not* made in proportion to the recipient's equity ownership of Class A stock.

These various withdrawals were entered in Towne's books as "Accounts Receivable—Miscellaneous." The entries on Spheeris' account were as follows:

Date	Debit	Credit	Debit Balance
May 27, 1953	$ 5,000.00		$ 5,000.00
Sept. 30, 1953	15,000.00		20,000.00
Oct. 28, 1953	16,500.00		36,500.00
Mar. 31, 1954	5,000.00		41,500.00
Apr. 28, 1954		$23,547.27	17,952.73
Apr. 28, 1954	25,000.00		42,952.73
Mar. 30, 1955	9,000.00		51,952.73
Apr. 27, 1955	5,000.00		56,952.73
May 24, 1955	3,000.00		59,952.73
Oct. 31, 1955	2,500.00		62,452.73
May 23, 1956		5,000.00	57,452.73
Nov. 30, 1957	1,500.00		58,952.73

The sole cash credit reducing Spherris' account in the *amount of $5,000 was in 1956, after* he was aprised that the present proceedings had begun. The 1954 credit of $23,547.27 was merely a bookkeeping transaction and did not represent a cash repayment by Spheeris.

None of the withdrawals was evidenced by promissory notes by Spheeris to Towne nor were they secured by any collateral. There was no provision for payment of interest to Towne; and, in fact, no interest was ever paid. No date of repayment was specified.

During the period in question, on advice of counsel, no formal dividends were declared by Towne. The Tax Court found that during such time there was doubt as to the tax effect on the corporation of a million dollar treble damage award it had received in an antitrust action. See, *Milwaukee Towne Corp.* v. *Loew's, Inc.*, 7 Cir., 190 F. 2d 561 (1951). Further, the status of United Artists as a stockholder was in doubt, following notice given in 1954 by Towne demanding that United Artists return its Class B stock because of the latter's alleged breach of contract.

After notice by Towne to United Artists to return the Class B stock, the latter filed suit in 1954 against Towne charging that Spheeris and other officers had mismanaged

the company and complaining of loans and advances made by Towne to Spheeris and other family stockholders. In answer to that complaint, filed prior to the instant proceedings, Spheeris and others admitted receiving loans from Towne. In addition there was testimony before the Tax Court by Spheeris and S. J. Papas that the payments in question were at all times considered by them as loans which were intended to be repaid.

From 1952 to 1956, Towne had substantial earned surplus, and the withdrawals in question were taken from earnings and profits.

After considering all the above facts and weighing the credibility of Spheeris and his witnesses in such circumstances, the Tax Court made its ultimate finding that the payments in question were not intended to be repaid as loans, but rather were dividends within the scope of the relevant statutes.

In reviewing the Tax Court's determination that the payments in question were taxable dividends, the problem before us involves "mixed questions of law and fact." We may review the legal effect of the facts found by the trier of fact.[2] *Ortmayer* v. *C.I.R.*, 7 Cir., 265 F. 2d 848, 854 (1959). The primary facts here are not in dispute, and we are not called upon to determine whether they find sufficient support in the record or are clearly erroneous as was the situation in *Zeddies* v. *C.I.R.*, 7 Cir., 264 F. 2d 120, 126 (1959).

In cases involving payments to stockholders, subsequent to advances to their corporation, where it is disputed whether such advances were loans or capital contributions, we have held that the subjective intention of the parties is a major factor in determining the legal relationship for tax purposes. *Jennings* v. *United States*, 7 Cir., 272 F. 2d

[2] *Cf.*, the "clearly erroneous" standard of review indicated in *Clark* v. *C.I.R.*, 9 Cir., 266 F. 2d 698, 710 (1959); *Lenasfield* v. *Commissioner of Internal Revenue*, 5 Cir., 21 F. 2d 508, 510 (1957); *Regensburg* v. *Commissioner of Internal Revenue* 2 Cir., 144 F. 2d 41, 44 (1944), cert. denied, 323 U.S. 783.

842 (1959). *Ortmayer* v. *C.I.R., supra.* Such intention may be ascertained from the testimony of witnesses and from objective manifestations of intent. No single indicium or criterion is conclusive. *Arlington Park Jockey Club* v. *Sauber,* 7 Cir., 262 F. 2d 902 (1959). Similarly here, the legal relationship between the closely-held corporation and its stockholders as to *these particular payments* must be established by a consideration of all relevant factors indicating the true intent of the parties.

After examination of the relevant facts, we agree with the Tax Court that the legal effect of the payments in question was to provide dividends to Spheeris. Numerous objective facts support this conclusion: none of the withdrawals was evidenced by promissory notes or secured by collateral; no interest was charged or paid; no dates for repayment were set and the single repayment came after the instant proceedings were initiated; no dividends were declared, but withdrawals were taken from the closely-controlled corporation as Spheeris and his family needed funds; and finally, prior loans made to Towne were evidenced by promissory notes and repaid with interest.

Petitioners point to several factors they feel indicate a contrary result: the testimony of Spheeris and S. J. Papas, the accounting entries in Towne's books, the fact that withdrawals were not made in proportion to stockholders' proprietary interest, and the statement in Towne's answer in the 1954 mismanagement suit that the payments were loans. However, in the particular circumstances here, such facts cannot overcome the proper inference that Spheeris was taking advantage of his position in a closely-held family corporation to provide himself with disguised dividends with nothing more than an accounting entry that such payments were loans and with no obligation to repay.

The decision of the Tax Court is affirmed.

AFFIRMED.

APPENDIX B.

Judgment.

UNITED STATES COURT OF APPEALS
For the Seventh Circuit

Tuesday, December 13, 1960

Before

Hon. John S. Hastings, Chief Judge

Hon. Elmer J. Schnackenberg, Circuit Judge

Hon. Latham Castle, Circuit Judge

Andrew M. Spheeris and Ismene A. Spheeris, Petitioners, vs. Commissioner of Internal Revenue, Respondent.	Petition for Review of a Decision of the Tax Court of the United States.
No. 13093	

This cause came on to be heard on the transcript of the record from the Tax Court of the United States, and was argued by counsel.

On consideration whereof, it is ordered and adjudged by this Court that the decision of the Tax Court of the United States entered in this cause on February 9, 1960, be, and the same is hereby, Affirmed, in accordance with the opinion of this Court filed this day.

APPENDIX C.

Order Denying Petition for Rehearing.

UNITED STATES COURT OF APPEALS
For the Seventh Circuit
Chicago 10, Illinois

Wednesday, January 25, 1961.

Before

Hon. John S. Hastings, Chief Judge

Hon. Elmer J. Schnackenberg, Circuit Judge

Hon. Latham Castle, Circuit Judge

Andrew M. Spheeris, et al., Petitioners, vs. Commissioner of Internal Revenue, Respondent. No. 13093	Petition for Review of a Decision of the Tax Court of the United States.

It Is Ordered by the Court that the petition for rehearing of this cause be, and the same is hereby Denied.

APPENDIX D.

Opinion of Tax Court.

(Not Printed)

Pursuant to Rule 23(i) we have not printed the Opinion of the Tax Court of the United States since we have submitted nine copies of the Record and the opinion is printed at pages 324 to 330, inclusive, of the Record.